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THE ATTITUDE OF THE STATE TOWARD RAILWAYS

A Discussion of the Question of Nationalization

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As a matter of practical politics, the problem of the desirable relationship of the state toward the railway has been settled in most countries of the world by the adoption of a policy of nationalization. In but three or four of the more prominent countries does the state take no part in railway management, and, in the case of England, one of the two great strongholds of independent railway enterprise, it is interesting to note that, in nearly all of her colonies, possessions, and protectorates, the imperial or colonial governments have freely undertaken the responsibility of railway management. The record of the last few years shows very clearly that the tide of railway nationalization is strong and steady. The acquisition, by the state, of the Western Railway of France, of the West of Flanders Railway of Belgium, of the railways of Japan and Switzerland, the extensive purchases of private lines by Austria, and the resumption of state operation by Italy, are examples in very recent years of the vigor and vitality of the movement. The forces underlying this development have been very complex. Political unity, social amelioration, industrial progress, and financial gain have all been influential motives, varying in relative intensity, of course, in different countries. If, however, one examines the history of that period from which the substantial growth of nationalization really dates, namely, the third quarter of the nineteenth century, the importance of political motives in promoting this movement is very conspicuous. Thus, in Belgium, as in Switzerland a quarter of a century later, the fear of foreign financial control of the railway system was a powerful factor in inducing the resumption of state activity in the railway industry. In Austria and Italy the relation of the state railway system to political harmony and to military strength was regarded as a very important one. Because of this fact, the rehabilitation of state railway systems inaugurated in the decade 1868 to 1878 must not be viewed as a vindication, justified by the history of the previous generation, of the economic benefits of state as against private management of railways. The record of state railway management up to that time had been a very discouraging one. In Belgium, for instance, for five years after

the opening of her first mileage, the state constructed and operated all railways, but the financial results were so unsatisfactory that the extension of the system was entrusted to private enterprise. In Austria and Prussia the inability of the state to secure adequate financial returns from its railways led to the temporary abandonment of the policy of state expansion. Similar experiences, it will be remembered, were the lot of certain states of this Union. There were no facts in 1870 which could be adduced to establish the economic advantage of state railway systems. On the other hand, there were conspicuous examples of the successful working of private roads in America, in England, and even in Continental Europe. At the very time when the Prussian Diet expressed itself in favor of continuing further with the project of a national system, private enterprise was clamoring for railway concessions, in spite of all restrictions that the government had imposed upon construction and working. One of the considerations that induced the Belgian government, in 1871, to resume its railway activities was the too successful competition of the private companies with the state lines. Some companies, it is true, had not met with success, but the financial failures of such roads seem to have been mainly due either to the excessive restriction of governments constitutionally inclined to paternalism or to the fact that they had been located, under the influence of the state, in regions of scanty population and poor economic possibilities.

Apart from ideas of the promotion of political unity or political aggrandizement, some fear was entertained that this new industrial power, promising to become of huge magnitude, might become a political danger, if left in private hands. The unconciliatory and undiplomatic spirit, manifested, at times, by some of the railway managers, served but to foment such a feeling. A more general influence in favor of the movement towards nationalization was the reaction against the *laissez-faire* teachings of the Smith school, which, by this time, had gained considerable strength, as is concretely evidenced by the economic congresses of Eisenach and Milan in the early and middle seventies. There was thereby induced a more favorable attitude towards the intervention of the state in the field of economic production than at any previous period of the century. Since that time the affection of the peoples of Continental Europe for government paternalism has, if anything, grown greater, and, as a whole, they are inclined to accept, without argument, the theory of the beneficence of state railways.

Nor is this feeling limited to these countries. Twenty-five years ago, Professor Hadley, in concluding his book on railway transportation, said, "There is a strong popular feeling, to a large extent unsuspected by those in authority, in favor of government ownership of railways as a system." Undoubtedly, in England and America, there are today, among the working classes particularly, strong leanings in this direction—the doctrinaire product of social idealism but nevertheless to be reckoned with in the near future. A similar, though less extensive, impression has apparently been made on other classes of society. I have sometimes wondered whether the large increase in the number of state employees, which has naturally accompanied the growth of entrepreneurial and regulative functions on the part of the state, has not had an appreciable influence upon public sentiment. The ideas of the majority of such employees as to the functions and capacity of the state are apt to be affected by their very relationship to it, and these would easily be disseminated, by their medium, amongst a considerable section of the public. This concept of the general beneficence of state policy has fostered the belief that, under the ultimate influence of state management, the railway system may be so organized as to promote the social amelioration and industrial progress of the community in a manner impossible under conditions of private operation. During the last generation, governments undertaking railway nationalization, and other advocates, have laid increasing emphasis upon this assumption. They have unrolled before their audience, the people, an attractive picture of railway systems without capital charges, levying minimum rates and fares, with innumerable resulting advantages for every one. To what extent this picture has found realization in actual conditions we shall shortly see. But however that may be, its influence on the progress of nationalization is unquestionable.

Interwoven with the strands of this medley of politics and social idealism, here and there appears the motive of artificial stimulation of economic development. The desire of relatively undeveloped communities to hasten the natural growth of their estates is not a surprising one, nor is it strange that they should select the state management of railways as their means to that end. Whether their object is best attained in this way is another matter. The construction of a larger amount of railway mileage may be thus secured, with attaching increments of traffic, but this does not in itself justify the policy. The direct financial losses usually

involved, the indirect losses arising from an arbitrary diversion of national resources of labor and capital from other interests, the effect of the distraction of the attention of the government from those very important elements of national welfare which are not economic, the possibility of the stimulation of private enterprise, under judicious supervision and with suitable aid, into the accomplishment of its aims, all need to be taken into full account; but, unfortunately, such communities rarely stop to cast a trial balance of gains and losses.

Such are some of the leading influences that have led toward nationalization, each one of which would form a most interesting study. Obviously, only the bare outlines of the general movement could be sketched in this paper, sufficiently distinctly, may the wish be expressed, to indicate that, from the point of view of permanent public welfare, there is still justification for further discussion of a problem which practical politics has declared settled.

The leading aspects of such a discussion are twofold, (1) the effect of the state upon the railway, (2) the effect of the railway upon the state. Under the former head falls the question of the financial remunerativeness of state railways, an important, though not conclusive, test of efficiency. Varying conditions of construction and operation render the correct application of this test a very difficult one. For instance, to attribute greater efficiency to Australian railways as against British railways, because of a 4 to 4½ per cent dividend as against a 3½ per cent would be ridiculous. Owing to the value of land, state regulations, and standards of construction, the capital per mile of railway in Great Britain is five times that of Australian railways, some of the recent extensions of which, by the way, have been made at the low figure of \$5000 per mile, sufficient to lay down but the flimsiest of tracks with the absolute minimum of facilities. Differences of capitalization and of rate levels may make interest rates incomparable things. A still further difficulty appears in the frequent unreliability of the financial statements of state undertakings of large capital and revenue accounts. The utilization of other state funds for the reduction of railway debt is an attractive financial manipulation which has notably vitiated the significance of quite a few capital accounts. Discussing the industrial domain, with particular reference to factories for the provision of army and navy supplies, Bastable says, "On purely financial grounds, state in-

dustries of the kind are open to serious criticism, owing to the very defective system of keeping accounts which is characteristic of such establishments. The amount of invested capital is hardly ever properly estimated; receipts that should go to capital are assigned to revenue, and expenditure that ought to be met from revenue is defrayed from other state funds or by borrowing." And as he reminds us in a footnote, Richard Cobden, in his last speech in the British Parliament, now some forty-six years ago, protested that, "Throughout the inquiries before Parliamentary committees upon our government manufactories, you find yourself in a difficulty directly you try to make the gentlemen at the head of these establishments understand that they must pay interest for capital, rent for land, as well as allow for depreciation of machinery and plant." In his illuminating articles upon the Belgian state railway system, published some four years ago in the *Revue Politique et Parlementaire*, M. Marcel Peschaud charged the state's system of railway accounts with the greatest confusion, credits relating to the railway having been distributed among five different budgets. Among other defects he noted the fictitious nature of amortization as represented in the railway accounts, with the result that, "it is not possible", he said, "to fix with accuracy the actual amount of capital expenditure, nor, in consequence, the real charges relating to this capital." This same element of fictitiousness in the amortization accounts appeared, he stated, in the Prussian Railway accounts. Elsewhere he remarked, "Nothing is more difficult than to ascertain exactly the financial results of a state enterprise. This is true, no matter what may be the country or the industry concerned. While simplicity and clearness of accounts are the law of private industry, complication, fiction, and obscurity are the rule in state industries." In state railways, therefore, we need apprehend no danger of understatement of capital percentages of surplus earnings, and while such figures, whether correct or incorrect, are not adequate indications of relative efficiency, they may still be used, in a rough sort of way, to throw some light upon the general financial productiveness of state railway systems.

Generally speaking, the results have been poor. For instance, in 1907, quite a favorable year for railway traffic, the state systems of Europe, excluding Prussia and Saxony, earned possibly 3 per cent upon their reputed capitals. Thus France (l'ancien réseau de l'État) made 1.87 per cent, Italy 2.18.

Norway 2.64, Sweden 2.75, Denmark 2.92, Württemberg 2.47, Austria 3.01, Belgium 3.29, Bavaria 3.45, Hungary 3.50, Imperial Railways of Alsace-Lorraine 3.58, Switzerland 3.62, Baden 3.90 per cent. In 1908, when the effects of the economic depression which commenced in the United States in the fall of 1907 really began to be felt, the average return fell considerably below 3 per cent. Such results indicate that most of these railways, on a proper representation of capital probably all of them, were actual burdens upon the finances of their respective states, for the latter have usually had to pay from $3\frac{1}{2}$ to 4 per cent, or even more, for the necessary capital. It has been urged that most of the state railway systems of Europe show little or no financial success because the governments have used their railways, not for purposes of gain, but for the promotion of trade and industry by low transportation charges. The argument is a very sophistical one. If this were a characteristic of state management, then the most important state railway administration, that of Prussia, would not have been paying dividends of 5, 6, and 7 per cent for the last thirty years. Bismarck, it is true, promised the Prussian Diet that, if the purchase of the private railways were authorized, railway surpluses should be used for improvement of the system, not for the financial benefit of the treasury. But fat railway surpluses have proved too much even for Prussian self-restraint, and the state has hugely enjoyed them. There is not a railway-owning government of Europe but would be glad to secure help to its national finances from the profits of railway working. The low railway charges of such countries, in so far as they are low, are to be largely credited to the irresistible pressure of very limited individual purchasing power. But while passenger rates are low, there is reason to doubt whether this can be said of freight rates, an adjustment which savors more of political expediency than of economic advantage. Attempts to make state railways more profitable have not been unknown. But recently, Austria and Hungary have appreciably raised their charges. Russia, Denmark, and other states, at different times, have made general increases, in some instances realizing to their discomfiture that such increases may destroy sufficient traffic to leave unaltered, or even to reduce, gross revenue. In countries where the average income of the great mass of the population is low, charges that appear low from the standpoint of, say, an American, may actually be as high as the traffic can be made to

bear. It is not denied that, in a number of instances, the taking over of private lines has been signalized by some reduction of rates and fares, a preliminary taste as it were of the future good things that the government had in reserve, but the process has hardly been a continuing one. Take, for instance, the state railway system of France as against the private companies, and one finds that, whereas, from 1888 to 1908, the state receipts per ton kilometre increased from 5.15 to 5.23 centimes, those of the private companies fell from 5.66 to 4.20 centimes. Even in passenger kilometre receipts, the favorite altar for the propitiatory sacrifices of government, the decrease in the state system was but $9\frac{3}{4}$ per cent as against 28 per cent in the case of the private companies. The passenger receipts of the state are still slightly the lower, though part of the difference can be put down to its appreciably higher proportion of third class traffic.

Saxony has had somewhat better fortune than the states just dealt with, for though the percentage earned on reputed capital was but 3.78 in 1908, for some few years preceding 4 and 5 per cent surpluses were the rule. Prussia, however, is the one example of marked financial success over a period of considerable length. This unusual achievement was favored by the fact that active state control was undertaken just about the time when the great economic advance of Germany was commencing. Financial prosperity was assured ahead. It is fair to inquire whether, under such conditions, the Prussian state railways have accomplished for the economic development of their country all that might reasonably have been expected from them.

Despite statistics showing the growth of the commerce and industry of Prussia, which prove nothing, as no one can tell what would have been the result with a different system of management, I am inclined to think that they have not done so. So far as my reasons for this opinion can be expressed in brief, they are as follows: Prussia is operating her railway system under peculiarly advantageous conditions—namely, compact territory, dense population, favorable physiographic conditions, unity of railway management arising from the fact of state operation, low labor cost, low taxation, a people temperamentally and by military training inclined to take severe restrictive control as a matter of course. For instance, Prussia has five times as many people per mile of line and twice as many miles of line per unit of area as the United States. The enormous physical obstacles to economical

operation offered by the Rocky Mountains are absent. The practical monopoly enjoyed obviates many expenses of organization and of competition for traffic. Taxes per mile of line are little more than half those of the United States. Railway labor-cost per individual averages about half that of this country. Add to these the high average intelligence of its people and the rapidity of economic progress, and all the elements of efficient and economical operation, making easy the combination of very low charges with high rates of profits, are present. Yet what has been accomplished? For one thing comes the reply, extraordinarily low passenger rates, rather less than one cent per passenger mile, in 1908, as against 1.9 cents in the United States. But there are several points to be noted in connection with this. In the first place, Prussia, with its denser population, affords to the railways a passenger density of four and a half times that of the United States, and such enormously greater density, in the case of traffic that handles itself, lowers the cost per mile very considerably. In the second place, the third, and especially the fourth class in Prussia, represent facilities which the average American traveler would not put up with for the small annual amount he would thereby save. In the third place, the cheapest accommodation that can be properly compared with that of American passenger trains, the second class, averages 1.6 cents per passenger mile, a charge which represents quite as much to the average German as 1.9 cents does to the average American. In the fourth place, though operating costs are low, there is ground for suspicion that Prussian fourth class rates are more helpful politically to the government than profitable to the railway. Passengers, however, bring in but 28 per cent or so of total operating income, while freight traffic produces about 65 per cent, a similar ratio to that of the United States. Moreover, of the two branches of the service, freight traffic is the one which calls for the exercise of most skill; it is also readily susceptible to reductions of cost. The Prussian Railway Department seems to have failed to realize its opportunities. From 1880-1908 freight transportation charges in Prussia decreased about 15 per cent; in the United States, during the same period, they decreased nearly 40 per cent. The average ton mile receipt of Prussian railways, in 1908, was 1.24 cents; in the United States .754 cents, nearly 40 per cent less, really about 60 to 65 per cent less if equivalent purchasing power be taken into account. The *Ausnahme* tariffs, covering wagon

loads of 22,000 pounds and over, and accounting for 21,144 million ton kilometres out of a total of 32,810 million, very largely coal, ores, lumber, stone, earth, raw materials and grain, worked out at an average receipt per ton mile of 90 cents, in spite of the depressing influence of political export rates, a figure very appreciably higher than the average for all classes of goods here. The normal tariffs for wagon loads, accounting for 9600 million ton kilometres, gave an average receipt of 1.5 cents per ton mile. These figures are only averages and easily liable to misinterpretation, but the differences indicated are so great as hardly to leave room for any doubt as to the superior economy of American freight transportation to its users. There is a much closer similarity in the general make-up of the tonnage than some writers have supposed. Nor can the difference in average haul have any greatly disturbing effect on the comparison, for the great bulk of the tonnage in both countries is low class carload traffic, loaded and unloaded by shippers and consignees. Terminal charges for handling this class of traffic are comparatively light, and therefore cannot be responsible for the difference of costs such as occurs in short and long distance hauls of freight that has to be loaded and unloaded by the railway. Then it has to be borne in mind, in connection with this carload freight, that increase in length of haul means increase in the number of division yards that have to be passed through, involving rehandling in the case of most trains; also that wages of enginemen and trainmen, cost of fuel and supplies, and cost of maintenance of rolling stock tend to keep pace, more or less exactly, with increase of haul. The density of freight traffic, it should be observed, is nearly the same in both countries.

Further, throughout the whole comparison, the different wage costs need to be borne in mind. In the United States, 60 per cent of total operating expenses is consumed by wages and salaries, and the average rate of pay of the American railway employee runs at least 100 per cent greater than that of Prussian employees, including all allowances and so forth. This means that, if American employees were paid on the same basis as Prussian, freight rates could be reduced to just half Prussian rates and passenger rates to the same level, while net income would actually be greater than it is now.

The contrast between the freight and passenger rates of Prussia is such as inevitably to create the impression that the former constitute more or less of a tax upon facilities, and this feeling

is emphasized when one bears in mind the severe restrictions, such as those of the demurrage and loading regulations, to which the freight traffic is subjected. It may be good political policy to maintain passenger fares at a low level, but, if this means that profits have to be bolstered up at the expense of freight charges, it is unfortunate. Since an infinitely smaller proportion of the income of the average individual is spent on railway passenger traffic than on freight transportation, low passenger fares are, in general, of much less economic importance to the community than low freight charges.

Like state managements in general, that of the Prussian railways seems to be inelastic. Some half dozen years ago, the Prussian operating ratio was about 62 per cent: it was 62.67 in 1905. In the three following years, it rose 12 points, reaching the unprecedented figure of 74.62. In France the increase was from 52 to 58, in England from 62 to 64; in the United States from 66.78 to 70. In all these countries the same economic influences were at work during the period, a general upward movement in the cost of railway labor and supplies, and, during the last year, the pressure of the financial panic which commenced abruptly in the United States towards the close of 1907. A similar relationship is revealed when the ratios of the state railway of France is compared with those of the five great private lines (the Western being excluded because of the embarrassment of its working by anticipations of purchase). The former increased its ratio from 72.2 in 1905 to 80.69 in 1908, while that of the latter lines increased from 50.2 to 54.8. I do not wish to make the mistake of laying undue emphasis upon figures which represent the results of the action of complex and varying combinations of forces, but such dissimilarities as do exist seem hardly capable of explaining away the criticism of state management involved in the comparison. One of the most eminent students of international railway policy, M. Colson, said but recently "*Les administrations d'État, généralement, (sont) moins habiles que les compagnies à serrer les prix de revient à découvrir et à réaliser toutes les économies possibles.*"

Yet, in some ways, the railway administration of Prussia has been inclined to push economy to the extreme. In 1906 an expenditure of \$50,000,000 on equipment was authorized, and much has been made of this action as an illustration of the advanced policy of enlightened state management. But, as a matter of fact,

the conditions of car service had become absolutely lamentable, and the government did not undertake this expenditure until it was actually unavoidable. The 1907 report of the Chamber of Commerce of Essen says "..... the increase of our roadway accommodations, and the provision of rolling stock, etc., has not taken place in a manner corresponding to the development and the necessities of traffic, and, further, no progress of general importance has been made in the matter of our goods traffic." Charges of this kind are common in the history of the Prussian state railways. Ten years ago, Professor Dr. Arthur Böhltingk, in his pamphlet "*Unsere Deutschen Eisenbahnen*", wrote "Although his Excellency Von Thielen has not once been able to provide sufficiently for the demands for rail transport, and although he has repeatedly declared that the railways had reached the limits of their capacity, he seems to have thought less than ever of making them equal to such demands by means of additions and improvements."

Short of an exhaustive analysis impracticable within the limits of this paper, sufficient evidence has been brought forward, perhaps, to indicate how little reliance can be placed upon the argument for nationalization which is based on the results of Prussian railway management. In spite of all its apparent success, I am convinced that the state government has failed to live up to its opportunities. With all the disadvantages and defects of the privately managed American railway system, and notwithstanding the restrictions placed upon its working by federal and state governments, it has contributed far more to national economic development than has the state system of railways in Prussia.

There are certain other features of state railway management, a brief statement of which must suffice, though their importance is considerable. There can be no question but that, where economic conditions render it at all practicable, state railways will endeavor to make profits. The history of Prussia indicates very clearly that, under such circumstances, there is a great probability of too intimate a relationship being established between the financial and railway departments of the state. This is likely to lead, as it has led in Prussia, to a subordination of the economic interests of the industry to the fiscal necessities of the treasury. Again, with the nationalization of the railway system, the experts of that branch of industry become government servants, and, as such, liable to less searching criticism than when, as the repre-

sentatives of private enterprise, the sword of government investigation and regulation was constantly suspended above their heads. Like individuals, government is not apt to criticise itself. The depressing effect of government management upon the initiative and self reliance of employees is an old charge, and I will do no more than quote from the report of the recent Board of Trade investigation of Italian railways. "There is one element in connection with the transfer from private working, and that is the change which has taken place in the management of the personnel. Numerous removals have been effected consequent on promotions being made in order of seniority, which is not in all cases compatible with merit. One hears traders who have had close associations with the officials, in the days of private ownership, deploring the disadvantages caused by the removal of local officials possessing intimate knowledge of the working, and their replacement by officials from probably quite a different part of the country owing to some claim of seniority. Again, in the staff themselves, there has been noticed, it is said, a change occasioned by the transfer from private to state ownership. As state officials, there does not seem to be quite the same amount of willingness to take responsibility; the strict letter of the rules and regulations is the boundary line over which there is no disposition to step."

So much for the influence of state management upon the railway. We may now ask what is the effect of the state railway upon general state administration. This question is worthy of a much more elaborate answer than I can possibly give at the present time, and I shall not attempt to do more than outline some of the leading considerations. First, then, the entry of the state into general or specific industrial competition with its own citizens is neither wise nor proper. Its natural position as the disinterested and unbiased dispenser of justice, revealer of frauds, and adjuster of inequities is prejudiced thereby. Confidence in its impartiality becomes weakened, capital hesitant, private initiative less keen, with corresponding retardation of the material growth of the community. Secondly, the duties necessarily imposed upon the executive of the modern state in connection with the fundamental functions of administration of justice, protection of the community from physical and moral violence, whether in social or strictly economic relations, and guardianship of its physical and mental health, constitute a heavy burden in themselves; and an efficient

discharge thereof is far from being attained in the most advanced countries. To superimpose upon these duties the responsibilities of the industrial entrepreneur is to diffuse the energies of the state through a still wider field, over which it is likely to exercise a still less satisfactory control. The capacity of government is not unlimited. Thirdly, in so far as the railways are productive of surpluses, to that extent the executive of the state is relieved from drawing upon the pockets of the taxpayers. It is admittedly difficult even in the most democratic states to keep the executive in responsive relationship to the legislature and to the public. The more dependent the executive is upon funds raised by taxation, particularly direct taxation, the less arbitrary can it become. The ultimate political well-being of the democracy rests upon the practical recognition of this canon of government. Fourthly, fiscal reliance upon railway earnings is apt to prove embarrassing to state finances, at recurring periods, from shrinkage of receipts—a difficulty that is accentuated by the apparent inability of government railways to adjust themselves readily to economic vicissitudes.

From the point of view either of the influence of the state upon the efficient management of the railway system, or of the influence of the responsibility of railway management upon the efficiency of state administration, there is reason to dispute the advantage so loudly claimed for nationalization. The real meaning of railway nationalization is the substitution of uncontrolled state management for controlled private management, and the change is unfavorable to economic progress and efficient government.